In the Supreme Court of the United States

OCTOBER TERM, 1965

No. 897

PIZITZ, INC., SUCCESSOR TO LOUIS PIZITZ DRY GOODS COMPANY, PETITIONER

v.

GEORGE D. PATTERSON, DISTRICT DIRECTOR OF INTERNAL REVENUE, BIRMINGHAM, ALABAMA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

MEMORANDUM FOR THE RESPONDENT IN OPPOSITION

The taxpayer, a department store, used the reserve method for computing deductions for bad debts, and on its income tax return for the taxable year ending January 31, 1960, claimed a $65,694.53 deduction for an addition to its bad-debt reserve. The Commissioner of Internal Revenue disallowed the entire deduction, on the ground that the taxpayer's existing bad-debt reserve ($173,295.81) was adequate. The taxpayer paid the resulting deficiency and instituted this suit for refund against the District Director of Internal Revenue, demanding a jury trial.

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At the close of the evidence, and after both parties had unsuccessfully moved for a directed verdict, the district court charged the jury that Section 166(c) of the Internal Revenue Code of 1954 provides that there shall be allowed, in the discretion of the Commissioner, a deduction for a reasonable addition to a reserve for bad debts, and that the burden was the taxpayer's to establish by a preponderance of the evidence that the Commissioner had abused his discretionary authority in this case. The jury found for the taxpayer. After a motion for judgment notwithstanding the verdict had been made by the Director and denied by the district court, the Director appealed. The court of appeals reversed the district court, holding that the evidence (Pet. Ex. A, p. 5) "does not rise to that level of proof which would show an abuse of discretion on the part of the Commissioner."

The decision of the court of appeals is clearly correct, and there is no conflict between circuits or other basis for review by this Court.

The taxpayer contends that the court of appeals redetermined the facts in violation of the Seventh Amendment. However, civil actions for refund of federal income taxes are not "suits at common law" within the purview of the Seventh Amendment although brought against the District Director of Internal Revenue. *Wickwire* v. *Reinecke*, 275 U.S. 101, 105–106. And, even where applicable, the Seventh Amendment does not deprive the courts of power to direct a verdict when the evidence is insufficient to warrant submission of an issue to the jury. *Balti-*

more & O. Line v. *Redman*, 295 U.S. 654. Since Rule 50(b) of the Federal Rules of Civil Procedure—the directed-verdict provision invoked by the Director in the district court—has been held to be consistent with the Seventh Amendment (*Galloway* v. *United States*, 319 U.S. 372, 389), so, clearly, is appellate review of the district court's refusal to grant a motion for a directed verdict.

As the court of appeals observed (Pet. Ex. A, p. 4), its review function was to determine whether the evidence, and the inferences drawn from the evidence, when viewed in a light most favorable to the taxpayer, justified submitting to the jury the question whether the Commissioner had abused his discretion.[1] It applied this standard correctly. The taxpayer's existing reserve of $173,295.81 was more than twice the amount of bad-debt losses which might be anticipated during the following year, in view of the taxpayer's own experience over the preceding five years.[2] And, though

[1] Since Section 166(c) contemplates the allowance of a deduction "in the discretion" of the Commissioner, the court of appeals properly distinguished (Pet. Ex. A, pp. 5–6) between the kind of evidence indicating that the Commissioner's determination was wrong and the kind of evidence—alone material—showing this determination to be so arbitrary as to constitute an abuse of discretion. See *Art Metal Const. Co.* v. *United States*, 17 F. Supp. 854, 862–863 (Ct. Cl.); *Maverick-Clarke Litho Co.* v. *Commissioner*, 180 F. 2d 587, 592 (C.A. 5); see, also, *United States* v. *Beckman*, 104 F. 2d 260, 262–263 (C.A. 3).

[2] The taxpayer does not deny that any excessive additions made to its reserve in prior years must be taken into account in determining the addition to be taken for the current year. Section 1.166–4(b), Treasury Regulations on Income Tax (1954 Code).

the taxpayer, in contending that its bad-debt experience in the past did not constitute a reasonable index to what the future might hold, cited strikes, automation, increasing delinquencies, and liberalization of its credit policies, all of these elements were present to a degree in the preceding five-year period during which its receivables and bad-debt losses remained relatively stable. (Pet. Ex. A, pp. 3–4; R. 84–85.) In these circumstances, the Commissioner's refusal to allow a further addition to the existing reserve was, if not clearly correct, certainly devoid of arbitrariness or any other element from which a jury could reasonably infer an abuse of discretion. Therefore, the court of appeals correctly ruled that the issue should not have been submitted to the jury.

It is respectfully submitted that the petition for a writ of certiorari should be denied.

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